

Internal Revenue Service  
Director, Exempt Organizations

Department of the Treasury

Person to Contact:

Identification Number:

Contact Telephone Number:

In Reply Refer to:

Date: OCT 24 2000

CERTIFIED MAIL

Dear Applicant:

We have considered your application for recognition of exemption from Federal income tax under section 501(c)(3) of the Internal Revenue Code. We have determined that you do not qualify for exemption under that section. Our reasons for our conclusion and the facts on which it is based are explained below.

You incorporated in [redacted] to operate exclusively for charitable and educational purposes within the meaning of Section 501(c)(3) of the Internal Revenue Code of 1986.

The mission of the [redacted] (hereafter referred to as "[redacted]") is to promote educational reform by changing the culture and climate within schools. To further this end, the [redacted] conducts the following activities:

1. Evaluation of the climate and culture within individual schools.
2. Provision of workshops and professional development to faculty and staff of participating schools.
3. Provision of curricula that promote character development to participating schools.

All services will be provided via the Internet and on site by paid consultants. Services will be provided to schools at cost- \$[redacted] per month per school.

Further clarification of your activities disclosed that you would research best-practice educational interventions and services. Identify appropriate services for schools, linking them to resources, and contracting with service providers. [sic]

[redacted] links schools with providers of evaluation, consulting and curricular services as necessary. Costs depend on the nature, scope and complexity of the services required by an individual school. Any revenues in excess of expenses will be distributed to exempt organizations established for educational purposes.



Awareness of [REDACTED] is created in several ways:

- ❖ You conduct informative, free seminars explaining our educational consulting services to schools and schools districts.
- ❖ You use [REDACTED] directory to mail directly to schools and districts.
- ❖ You make appearances at the local service clubs to inform them of your service.
- ❖ You are just finishing [REDACTED]'s first book entitled "[REDACTED]", scheduled for publication in July. You are working with a publicist who will schedule interviews in the paper, television, and radio talk shows. [sic]

You also stated, "The purpose of the book (which is not completed) will be to be used as a marketing tool to give to our prospects. It is currently a low priority however, and may not materialize. [REDACTED] acts as an umbrella organization, which utilizes successful programs from various sources. These are not owned by [REDACTED]. An example would be a school, which, during our consulting, expresses an opinion that it wants to place additional emphasis on reading and math. We may recommend [REDACTED] program out of [REDACTED], which has an excellent program in these areas. The actual cost would be determined by [REDACTED], a purchase order submitted, and upon funding, paid directly to [REDACTED] for the units purchased."

Clarity was requested of [REDACTED]'s relationship with [REDACTED]. You stated, "[REDACTED] is the name of the program and because of confusion between the two names, we are changing our corporate name to [REDACTED]"

[REDACTED]'s (aka, [REDACTED]) fee schedule disclosed that you charge from \$[REDACTED] to \$[REDACTED] per school for [REDACTED] which consist of on site visits, evaluation components and problem solving process training/tool kit. [REDACTED] consist of classroom management manuals, training and license fees are \$[REDACTED] per teacher, \$[REDACTED] per school and \$[REDACTED] per school. Phase [REDACTED] character education curriculum, training/implementation and license fees are \$[REDACTED] per grade level, \$[REDACTED] to \$[REDACTED] per school. You also provide customized training at \$[REDACTED] per hour session.

We are an education consulting firm. [REDACTED] has designed an evaluation of teacher attitudes, which is administered to schools at the outset. That survey will reflect both strengths and weaknesses in a given school. Once identified, we train the leadership and staff of the school on problem solving techniques and specifically on those areas, which were identified as a weakness. All of our materials are on our website, ([REDACTED]), including the training modules needed by the school. Since each school is different in its needs, we design a solution specific to that school. Because each model is unique to each school, there is no "retail" cost but rather actual costs of subcontractors plus our fee. We do add on a management fee of usually [REDACTED] % [REDACTED].

Section 501(c)(3) of the Internal Revenue Code provides for exemption from Federal income tax for organizations which are organized and operated exclusively for charitable, religious, and educational purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Section 502 of the Internal Revenue Code provides that an organization operated for the primary purpose of carrying on a trade or business for profit shall not be tax exempt on the grounds that all of its profits are payable to exempt organizations.



Section 1.501(c)(3)-1(a)(1) of the Income Tax Regulations provides that in order to qualify for exemption under section 501(c)(3), an organization must be both organized and operated exclusively for one or more exempt purposes. Failure to meet either the organizational or operational test will disqualify an organization from exemption under section 501(c)(3).

Section 1.501(c)(3)-1(c)(1) of the Regulations provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which accomplish such purposes. An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose. Thus, in construing the meaning of the phrase "exclusively for educational purposes" in Better Business Bureau v. United States, 326 U.S. 279 (1945), the Supreme Court of the United States stated, "This plainly means that the presence of a single non-educational purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly educational purposes."

Section 1.501(c)(3)-1(e)(1) of the Regulations provides that an organization may meet the requirements of section 501(c)(3) although it operates a trade or business as a substantial part of its activities, if the operations of such trade or business are in furtherance of the organization's exempt purpose or purposes and if the organization is not organized or operated for the primary purpose of carrying on an unrelated trade or business as defined in section 513. In determining the existence or nonexistence of such primary purpose, all the circumstances must be considered, including the size and extent of activities, which are in furtherance of one or more exempt purposes.

Section 1.513-1(d)(2) of the Regulations provides that a trade or business is "related" to exempt purposes only where the conduct of the business activity has a causal relationship to the achievement of any exempt purpose, and is "substantially related" for purposes of section 513, only if the causal relationship is a substantial one. Thus, for the conduct of a trade or business from which a particular amount of gross income derived to be substantially related to purposes for which exemption is granted, the production or distributions of goods or the performance of the services for which the gross income is derived must contribute importantly to the accomplishment of those purposes.

In B.S.W. Group v. Commissioner, 70 T.C. 532 359 (1978), the court held that an organization that provided management and consulting services to nonprofit organizations at fees set to cover costs and yield a 10.8 percent profit was not organized and operated exclusively for charitable and educational purposes. Furnishing the services at cost or above cost lacked the donative element to be considered charitable. The court also stated that the presence of substantial profits constitutes evidence that an organization is operating for a commercial rather than exclusively educational purpose.

Revenue Ruling 72-369, published in Cumulative Bulletin 1972-1, on page 245, holds that an organization formed to provide managerial and consulting services at cost to unrelated exempt organizations does not qualify for exemption under section 501(c)(3) of the Code. An organization is not exempt merely because its operations are not conducted for the purpose of producing a profit. To satisfy the operational test of the Regulations, the organization's resources must be devoted to purposes that qualify as exclusively charitable within the meaning of section 501(c)(3) of the Code. The organization was not exempt because it was carrying on a trade or business of the type ordinarily carried on for profit.



4

[REDACTED]

In reviewing the information submitted we hold that you have failed the operational test and do not operate within the purview of 501(c)(3) of the Code.

While you state that you are educational, although no documentation was submitted to substantiate your claim, the primary purpose of your organization is to act as an "agent" for other businesses and to operate a management/consulting firm. Accordingly, your organization is a commercial business.

Based upon the cited precedence, we have concluded that you do not qualify for exemption from Federal income tax as an organization described in section 501(c)(3) of the Code. In accordance with this determination, you are required to file Federal income tax returns on Form 1120.

Contributions to your organization are not deductible by donors under section 170(c)(2) of the Code.

In accordance with the provisions of section 6104(c) of the Code, a copy of this letter will be sent to the appropriate State officials.

If you do not agree with our determination, you may request consideration of this matter by the Office of Regional Director of Appeals. To do this, you should file a written appeal as explained in the enclosed Publication 892. Your appeal should give the facts, law, and any other information to support your position. If you want a hearing, please request it when you file your appeal and you will be contacted to arrange a date. The hearing may be held at the regional office, or, if you request, at any mutually convenient district office. If someone who is not one of your principal officers will represent you, that person will need to file a power of attorney or tax information authorization with us.

If you don't appeal this determination within 30 days from the date of this letter, as explained in Publication 892, this letter will become our final determination in this matter. Further, if you do not appeal this determination in a timely manner, it will be considered by the Internal Revenue Service as a failure to exhaust administrative remedies. Section 7428(b)(2) of the Code provides, in part, that "A declaratory judgement or decree under this section shall not be issued in any proceeding unless the Tax Court, the Claims Court, or the district court of the United States for the District of Columbia determines that the organization involved has exhausted administrative remedies available to it within the Internal Revenue Service."

Appeals submitted which do not contain all the documentation required by Publication 892 will be returned for completion.

If you have any questions, please contact the person whose name and telephone phone number are shown in the heading of this letter.

Sincerely,

  
Steven T. Miller

Director, Exempt Organizations

Enclosure: Publication 892

cc: [REDACTED]